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QUESTIONS ON FEDERAL - PROVINCIAL ECONOMIC CO-OPERATION

STATEMENT BY

THE HONOURABLE

WILLIAM G. DAVIS

PRIME MINISTER OF ONTARIO


TO THE

MEETING OF FIRST MINISTERS

OTTAWA, NOVEMBER 15 - 16, 1971



ONTARIO



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INTRODUCTION

As you know, Mr. Chairman, the Government of Ontario is profoundly concerned by the weakened state of federal-provincial economic policy co-ordination and fiscal relations. Consequently, it is our considered belief that the First Ministers and their Ministers of Finance must undertake immediately a thorough overhaul of inter-governmental economic and fiscal relations. Our objective should be to provide a viable basis for the development of effective economic and social policies in the future. To this end, the Government of Ontario has advanced recently a comprehensive series of proposals for consideration by the federal and other provincial governments at this conference.

First, on October 14th I issued An Economic Strategy for Ontario which dealt with the major economic problems confronting Canada and our views on the development of new objectives and long-run economic policies. Second, my colleague, the Hon. Darcy McKeough, Treasurer of Ontario, presented to the recent Ministers of Finance Meeting the document The Reconstruction of Economic and Fiscal Policy in Canada. This paper contained our detailed appraisal of the current state of economic policy co-ordination, taxation and social security reform and fiscal arrangements, and advanced a series of proposals for fundamental improvements in each area.

These proposals were not advanced in a spirit of disruption, but rather as a frank evaluation of national economic policy operations over the past few years. And I say "national" rather than "federal" because we are speaking of the total fiscal framework of the federal government, the provinces and the municipalities. National fiscal policy must be the product of close intergovernmental fiscal co-ordination.

At this point I must emphasize that many of the views and proposals in these papers have been presented previously to various federal-provincial conferences over several years. Our reason for restating our earlier propositions is simply that we believe they have not been given adequate consideration by the federal government, and the reconstruction of intergovernmental policy and fiscal structures is now a matter of critical urgency.

As I have said, Mr. Chairman, the Government of Ontario has issued these two papers, so that they could be considered adequately by the federal and other provincial governments in advance of this conference. In the remainder of this paper, therefore, I shall confine my remarks to highlighting our main thoughts on the two agenda items covering the economic situation and fiscal arrangements. In particular, I will be asking a series of questions concerning the federal government's intentions and responses to Ontario's earlier proposals.

I THE ECONOMIC SITUATION AND UNEMPLOYMENT

It is my hope that, now the economy is beginning to show signs of positive recovery, many of the operational disagreements between governments on fiscal policy co-ordination can be laid aside and that we can concentrate on some of the major long-term issues that confront Canada. To this end, we have some proposals to put to the federal government today and we would also like to table some questions. The answers to these questions would, we think, help to clarify the direction of public policies in future years and also help provincial governments to develop their most appropriate roles.

1. Establishment of a Joint Economic Committee

There is a need for fundamental reform in the process of setting national economic goals and co-ordinating government fiscal policies to realize these goals. This overriding need was asserted both by myself on October 14, and by my colleague, the Treasurer, in his document, The Reconstruction of Economic and Fiscal Policy in Canada, presented to the November 1 Meeting of Ministers of Finance. It concerns me a great deal that we have no intergovernmental body to review and determine, on a continuing basis, national economic goals of a strategic order. The present structure of federal-provincial ministerial meetings and technical committees simply does not work effectively towards this end. Canada faces some very serious problems that require continual high-level liaison on national goals, economic

policy options and the technical means for their attainment. I would like to propose, therefore, that we, in this First Ministers' Conference, formally constitute ourselves as a national Joint Economic Committee with Finance Ministers as our representatives. I ask, therefore,

Does the federal government agree to the establishment
of a federal-provincial Joint Economic Committee?
If so, is it prepared to take a leading role in making
such an institution effective?

2. Immediate Policy Concerns

There are three areas of immediate concern that such a Joint Economic Committee should examine: the role of the provinces in economic stabilization; co-ordination of federal and provincial winter works programs; and, the establishment of a permanent program framework to deal with the special problems of seasonal unemployment.

The thrust of fiscal and economic policies in Canada is now settled firmly in the direction of expansion. I fully expect, however, that there will be a lagged response before full employment is reached. The experience of the past two years raises two specific problems which the Joint Economic Committee must consider. First, Ontario and other provinces find themselves in a very difficult fiscal position as a result of the slowdown in economic growth and government revenues.

Second, the provinces have been obliged to take on a disproportionately large role in policies for economic expansion. In this regard I would draw attention to Ontario's record budgetary deficits, its seasonal employment programs, its tax reductions and incentives to promote economic recovery. I ask, therefore,

Will the federal government take into account, in upcoming tax sharing negotiations, the major provincial contribution to economic stabilization during the recent slowdown? Furthermore, what is the federal government's view of the appropriate provincial role in future stabilization actions and the steps that should be taken to ensure concerted and co-ordinated federal-provincial policies?

I am also very concerned by the existence of independent federal and provincial winter works programs to deal with a common problem. We proceeded to implement our own winter works program because, until mid-October, the federal government gave every indication that there would be no winter works program this year. Now that a federal program has been announced, there is obvious duplication and potential overloading, particularly on the municipalities who must make these programs operational. I ask, therefore,

Will the federal government turn over to Ontario an appropriate share of the Local Initiatives Program funds and allow us to use these funds within the structure of our Municipal Incentives Program?

A further defect of the federal winter works program is the continuation of Special Development Loans. This is the second year in a row we have been invited to borrow money from the federal government for narrowly defined capital programs which entail close federal auditing. The Ontario Government has demonstrated through its major discretionary fiscal policies in the past two years that it can be trusted to act responsibly. We object to the administrative and economic rigidities of these Special Development Loans and also to the principle that provinces should assume long-term debt obligations to the federal government to relieve the consequences of federal fiscal and monetary policies. I ask, therefore,

Will the federal government remove the auditing restrictions, open up the eligible expenditures to include non-capital projects, and provide such funds to the provinces interest free?

I am also very concerned about the increasing number of young people entering the labour force each year without the prospect of stable long-term employment. To deal with this problem in a co-ordinated manner requires a permanent and joint governmental capacity

to launch special winter works and summer programs which can be accelerated or decelerated by mutual agreement each year, as proposed by the Treasurer of Ontario at the last Meeting of Ministers of Finance. I ask, therefore,

What is the federal government thinking on the problem of job prospects for young people?

Is the federal government prepared to sit down with the provinces, under the aegis of the Joint Economic Committee, to establish a permanent and pre-planned seasonal employment program in the immediate future?

The lack of business confidence in new government policies is also of immediate concern to Ontario. One of the contributing causes of our unsatisfactory economic performance has been in the intangible, yet vital, factor of business confidence. It is important that the private sector should have confidence in government policies which affect the long-run competitiveness and expansionary momentum of our businesses. The federal tax reform legislation has not generated confidence and support in the business community. Rather, it has created major uncertainty and a wait-and-see attitude towards investment decisions. The restrictive international provisions of Bill C-259, in particular, have generated apprehension among our largest businesses and a widespread concern that Canada no longer will be an attractive base for international operations. The Senate Committee on Banking, Trade and

Commerce expressed this very concern in its recent interim report on Bill C-259. The Ontario Government also believes that these new international tax rules will be detrimental, particularly to our multi-national companies, and will undermine Canada's long-run economic growth potential. I repeat Ontario's earlier request, therefore, that the federal government withdraw and revise the international sections of Bill C-259.

Is the federal government prepared to do this?

If not, is the federal government willing to assure Canadian companies that these new international tax rules will not result in higher taxes on legitimate foreign investment and business operations abroad?

Again, if not, is the federal government prepared to defend a tax regime which deters the establishment of multi-national companies in Canada and leads to the transfer of existing companies and existing jobs out of Canada?

Another contributing cause to current business uncertainty and reluctance to invest and expand is Bill C-256, the new Competition Act being advanced by the federal government. It seems inconsistent and inappropriate to me, at this time of intensified international competition, to enact legislation which discourages initiatives, thwarts potential mergers to achieve economies of scale, and imposes rigid and impractical constraints on the normal business practices of

Canadian companies. Rather, the thrust of reform in this area should be to encourage practical competition which benefits Canadian consumers, which imposes minimum restrictions on the proven free-enterprise system, and which permits Canadian businesses to compete on even terms with foreign competitors. The Ontario Government does not agree that we can afford the luxury of a policy that encourages industrial fragmentation and penalizes business practices which are the competitive norm in other countries with whom we must increasingly compete. I ask, therefore,

Is the federal government prepared to amend Bill C-256 to remove these undue restrictions and to preserve the ability of Canadian companies to compete effectively in the world market place?

3. Long-Term Economic Strategy

I would like the federal government to place before this meeting its views on the long-term policy problems facing the Canadian economy. The provinces have a lot at stake in these emerging areas of economic change. I would ask, therefore, whether the federal government intends to accord the provinces full consultation and participation in these important matters. I have six questions to ask in this regard.

- . Is the federal government prepared to take the provinces into its confidence on the matter of trade negotiations with the United States covering the auto pact, energy exports, and "concessions" which Canada may offer?
- . Has the federal government developed a tax strategy in response to export subsidization devices and generous tax rules such as DISC and VAT being employed or devised by other countries?
- . Is the federal government prepared to release to the provinces the Gray study on foreign ownership, and to formulate joint policies with the provinces in this priority area?
- . Has the federal government developed a new incomes policy or other contingency plan to combat renewed inflation, and, what role in such plans does it see for the provinces?
- . Does the federal government have a viewpoint and an economic plan on industrial consolidation to exploit economies of scale and allow Canadian companies to compete with industrial giants abroad?

- . Is the federal government satisfied with the results of its present policies to reduce regional economic disparities? Given the need to conserve national fiscal resources, and to use them in ways which produce maximum economic growth for Canada as a whole, is the federal government considering alternative policies?

II FISCAL ARRANGEMENTS

Although the agenda item for this meeting is somewhat vague on fiscal arrangements, I assume that, in line with our official Statement of Conclusions at the Victoria Conference, we are here "to discuss all aspects of these arrangements, including tax reform, shared-cost programs, equalization and tax sharing".

1. Tax Reform

I am pleased that the federal government has responded positively to our plan to establish a system of tax credits in Ontario. We are convinced that tax credits along the lines proposed by Ontario are the best and fairest vehicle for achieving redistribution of total tax burdens -- federal, provincial and municipal -- and for delivering real reform benefits to our poorest families and individuals. It is my hope that in future such a tax credit system will be incorporated within the national tax structure for the benefit of all Canadian taxpayers. In the meantime, I thank the federal government for agreeing to use its tax collection machinery to implement our tax credit plan for Ontario taxpayers. I would hope that, after full discussion between our respective officials, Ontario's tax credit system can be incorporated in the new tax collection agreement and put into effect for the 1972 taxation year.

2. Social Security Reform

In the related area of social security policy and tax reform, however, I am still greatly concerned about the lack of a co-ordinated overall approach by the federal government. The Ontario Government has consistently stressed the need for a comprehensive redistribution philosophy in which income security programs are properly meshed and integrated with changes in tax burdens. Instead, the federal approach continues to be a piecemeal and haphazard one of piling changes in family allowances on top of changes in unemployment insurance and changes in income taxation. The dangers of such unco-ordinated reforms and their undesirable effects on incidence were clearly demonstrated in a paper tabled by the Ontario Treasurer at the Finance Ministers' Meeting in mid-July of this year. Senator Croll's committee obviously appreciates the interrelationship of tax and social policies by emphasizing the need for a comprehensive approach to the problems of poverty and income redistribution. I ask, therefore,

Is the federal government willing to re-examine jointly with the provinces the whole subject of social security, tax reform, and income redistribution policies before proceeding with its family income security proposals? and,

Will the federal government agree to negotiate in an integrated manner all changes in tax and social security policies through the office of the Treasurer of Ontario and Minister of Economics?

3. Tax Sharing

In reviewing the record for the past five years of federal-provincial financial arrangements, I am impressed with the need for relatively drastic, yet very simple changes in these arrangements. At the last Meeting of Finance Ministers, the Ontario Treasurer and Minister of Economics stated in considerable detail my Government's findings on this matter and our specific proposals for the future. As I see it, the current arrangements fail to come to grips with the basic imbalance in our federal system between expenditure responsibilities of our respective governments and the distribution of the total tax resources our economy can be reasonably expected to generate. This is a pivotal problem, which needs to be resolved if undue and disharmonious tax levels are to be avoided.

With regard to tax sharing, the Ontario Government is seriously concerned that the federal government has:

- . changed the whole principle of tax sharing and reduced the provincial share of income and wealth taxation;
- . rejected or ignored the findings of the 1966 and 1970 Tax Structure Committee studies substantiating the fiscal imbalances in our present system;
- . used its own superior financial strength to force the provinces into new expenditure commitments, e.g. medicare;
- . made pre-emptive tax moves, like the Social Development Tax, which has been built into the new income tax system;

- . reiterated its creed that the provinces go out and increase their own taxes; and,
- . offered "concessions" in its revenue guarantee which add up to higher total tax rates on individuals.

Throughout these points, I detect a serious lack of concern on the part of the federal government for the total tax burden on our economy. I would like to ask, therefore,

Does the federal government have a view about the maximum size of the government sector and the total tax burden the economy is able to support at present and hopefully improving standards of living? and,

In view of such constraints, is the federal government willing to reconsider seriously the existing distribution of tax resources?

4. Cost Sharing

The present ponderous structure of cost-sharing programs is inefficient, an impediment to cost control and service improvement, and merely reflects the chronic and worsening imbalance to which I have already referred.

Briefly, a number of points can be raised on the whole question of cost sharing:

- . virtually all shared-cost programs have matured and acceptable national standards are well entrenched throughout the country;
- . the federal role has become a purely financial one, reflecting the inadequate distribution of tax resources;
- . the primary concern remaining is that of excessive cost escalation and the related question of improved efficiency and delivery of service.

Given these points, it is obvious that we have to increase provincial flexibility in these major areas of provincial jurisdiction and minimize cumbersome administrative structures. Ontario has suggested, therefore, that cost sharing be discontinued, and provinces be given full responsibility in these areas in exchange for equivalent financial resources. This procedure would greatly reduce the administrative burden, eliminate the special status of these programs, and reduce pressures on the total tax burden in our country. I ask, therefore,

Is the federal government willing to incorporate in the new five-year agreement provision for any province to assume full financial responsibility for existing shared-cost programs, if it so desires?

5. Regional Disparities

Federal government efforts to reduce regional disparities through revenue equalization payments and a host of other costly programs have shown few if any positive results, yet are likely to have been a major factor in dragging the whole economy significantly below its potential. The complexities of the current approach defy analysis and ways must be found to realize the objective of reducing disparities by more effective means without reducing the well-being of all.

Ontario does not question the real need for large-scale interregional transfers. Ontario has and always will support the objective of reducing interregional disparities. However, we are concerned that the trend in the present approach to this problem would serve neither the "have-not" nor the "have" regions of the country. If indeed these fears are justified, all eleven governments around this table have a genuine interest in critically examining the current structure and looking for superior alternatives. I believe, that we all need to examine this question with an open mind and, if necessary, admit that we have tackled this problem in the wrong way. It could well be that we require a drastically different approach. One thing is clear to me. At the present time, our efforts to reduce regional disparities come in the form of too many different and unrelated policies to be easily assessed for their impact.

I believe, we are all conscious of the various limitations in the current approach to equalization. For instance, the existing formula would fail to recognize the sudden and adverse impact of a more restrictive national resource policy on provinces such as Alberta, with the result that the cost of policies inspired by national interest would be borne on a narrow and inequitable basis. At the same time, it is clear that even the recipient provinces are not happy with many aspects, only one of which is the lack of positive results. I would like to ask, therefore,

Does the federal government share the provincial concern for the shortcomings and the lack of concrete results from the current redistribution system? and,

Is the federal government willing to undertake with the provinces a joint examination of its redistribution programs with a view to assess their overall impact and effectiveness and, if necessary, to develop a totally new approach?

III CONCLUSION

I believe that nothing short of a major reconstruction of economic and fiscal policy is essential in Canada today. We are prepared to make every effort to achieve that goal. Let us frankly admit where we have been wrong and seek to create a system that sustains us in pursuit of long-term economic growth and stability.

